Episode 207: Your Tax Questions Answered: 401(K)s, Roth Conversions, and RMDs

Tue, Dec 02, 2025 3:33PM • 40:58

SUMMARY KEYWORDS
Roth conversions, qualified distributions, rule of 55, 401(k) withdrawals, tax strategy, retirement income, financial personality, tax brackets, standard deduction, tax planning, investment strategy, demographic trends, interest rates, safe withdrawal rate, financial planning.

SPEAKERS
Briana Corbin, Wade Pfau, Alex Murguia

Briana Corbin 00:00
The purpose of retire with style is to help you discover the retirement income plan that is right for you. The first step is to discover your retirement income personality. Start by going to risaprofile.com/style, and sign up to take the industry's first financial personality tool for retirement planning.

Briana Corbin 00:38
and we're back from the Thanksgiving break and picking up right where we left off with another round of listener questions this week. It's all about the details, Roth conversions, qualified distributions, and why the rule of 55 isn't as simple as it sounds. Wade and Alex are here to help you shake off the turkey fog and sharpen your retirement tax strategy.

Alex Murguia 00:58
Hello everyone. Welcome to retire with style. I'm Alex, and I'm here with my trusted companion, Wade Pfau, and in this episode, we'll do a best impersonation of radio call in hosts as we do our Q and A sessions, right?

Wade Pfau 01:15
Wade, that's right, and this is a matter of over the summer, we had quite a few Q and A episodes, and we had a long backlog of questions we hadn't gotten to. So we're playing catch up, and we're trying to work our way through the backlog of questions that came in to make sure we get everything addressed, no,

Alex Murguia 01:33
100% and for those of you, just keep on sending them, we will get to them and they they're great for like, content ideas for us. So even though we may not hit the question immediately, we keep abreast of it, because we do try to keep a pulse of what folks are asking. Because it just behooves us for our sister firm, McLean, asset management, our online membership site, retire

with retirement researcher, and then it helps us with just content and research that we're always looking into.

Wade Pfau 02:02
Yeah, that's right. We may not answer the question today, we may not answer the question tomorrow, but Sunday and for the rest of your life,

Alex Murguia 02:09
we will. That sounds like what you tell somebody, Wade, When? When? If your wife asks you, hey, Wade, it's recycling. Put it outside in the front are you like, Yes, I'll get to it. I'll get to it.

Wade Pfau 02:20
That sounds like my kids. It sounds like they don't do it immediately. They're never going to do it. Oh, really. Oh, they'll forget.

Alex Murguia 02:27
Well, hopefully you can be a good example with with these questions. We're getting forgotten.

Wade Pfau 02:32
We're just taking our sweet time with it.

Alex Murguia 02:37
All right, here we go. Let's kick it off. I'll throw you a softball. You ready? Okay, I like your podcast, but I can't find a list of all the episodes. Is there a complete list of all the episodes available?

Wade Pfau 02:51
Yeah, we thought we'd start with that question. That's the only one that's meta, so to speak. But let me answer this way you can

Alex Murguia 03:02
actually yes, go to retirewithstyle.com and there, that's the website for for this podcast. And we're actually going to start really filling that up with a lot of cool stuff. But there, we do have a list of all the episodes that that you would ever want to listen to, all the news that's fit to speak

Wade Pfau 03:23
and that may be new since the question was asked, but indeed, all past episodes are available@retirewithstyle.com

Alex Murguia 03:30
and again, goes without saying, but you can subscribe to everywhere where they syndicate podcasts such as, you Know, Spotify, the apple one, et cetera, et cetera. We're everywhere, so you should be fine if you wanted to subscribe and get updates to it,

Wade Pfau 03:48
that's right. Okay.

Alex Murguia 03:50

All right, all right. So let's get to the meat of the sandwich immediately. That bread was wafer thin,

Wade Pfau 03:58
and the questions for this episode, we're putting them in themes, so that it's not just completely random. We're doing more distributions from qualified accounts, and Roth conversions is kind of a theme for this week.

Alex Murguia 04:10
Yeah, we're going to hover around those questions. So the first one is a doozy, and we'll break it up into four parts as our not a surprise considering our readers and listeners, they really get down in the in the you know, well served in the details, because that's where the devil is right, and you need to get that out. So the first question is, I have in per in quotations rule of 55 questions. I left employment of Company A when I was 55 and understand I could withdraw from that 401, K, without penalty, prior to 59 and a half, under the IRS rule of 55 after a short period of unemployment, I began working with Company B, where I have a new. 401, K, I did not roll for 1k money into a to b yet, from A to B, yeah, sorry, from A to B yet, because he doesn't like the options in B, nor have I actually withdrawn any money from a. So the questions today, while employed at B, can I still make penalty free withdrawals from the company. A 401, k, if I choose. If yes, never mind. Go ahead. Yes.

Wade Pfau 05:29
So right, this is like exceptions to the early withdrawal penalty, and the concern is, before you're age 59, and a half, if you take distributions from qualified accounts, you pay a 10% penalty unless there's an exception. And right now, we're talking about the exception that only applies to an employer plan from a particular employer. If you leave employment after age 55 it's not you left earlier and wait till you're 55 if you left employment after 55 then you can take penalty free distributions from that plan assuming they allow it. And that's an important caveat. The employer plans have the flexibility to decide whether they allow discretionary withdrawals or not. So assuming they allow it, you can distribute from that plan without penalty. And yes, that's true. It's okay if you go to work again somewhere else, there's no check about anything like that. You are still eligible. Even if you return to employment at Company B, you are still eligible to make penalty free distributions from your 401, K that you had with employer a, okay,

Alex Murguia 06:34
wait, and just something you said, I want to make sure it's understood. Okay, what if you retire at 53 and then you know you're 55 you had said something. I just want to make sure that's understood.

Wade Pfau 06:45
Yeah, that's not a you can't you have to leave employment when you're 55 or older. You can't leave earlier and wait until you're 55 so that's an important part of the rule that I think people might overlook. You have to leave employment at 55 or higher to be eligible for this exception.

Alex Murguia 07:04
Okay, so the next question, as a quadruple parter, if I leave B before 59 and a half, can I make penalty free withdrawals from both A and B for one case, assuming he's still contributing to the B,

Wade Pfau 07:23
well, assuming you had, yeah, made contributions, right? You're pretty busy here, because in this four and a half window a year window, you left the company, he's coming and going, there's probably not a lot in your account with B, but, but yes, there. There's no rule that you can only do it with one so if both plans allow the distributions. You could take distributions from both plans without penalty, given that you're over 55 when you left. So then

Alex Murguia 07:49
it stands to reason, just because it is a little echo of the first question, if you're 57 working in Company B, taking withdrawals from Company A, you can also make contributions to Company B, right?

Wade Pfau 08:05
Yeah. And this question seems like it's more in theory in some way than because, if you're working again, why are you wanting to make distributions from company?

Alex Murguia 08:15
But yeah, that someone's listening could kind of come up with. And so just to close the, you know, close any loops that could be open, is the only reason I'm asking it.

Wade Pfau 08:31
Yeah, that wasn't you're asking an extra question. But I don't think that's a problem. Like, I don't know that in practice, you'd want to be taking distributions from company A and making contributions to Company B, especially if you didn't like the options and company B, I don't disagree.

Alex Murguia 08:49
I'm just asking, and in case somebody is like, you know, on their elliptical thinking, hey, what about this? That's the only reason.

Wade Pfau 08:56
I think that's that's almost like a harder way to do a rollover to Company B.

Alex Murguia 09:00
Yeah. All right. Is there a limit to the number of 401 k1's can make rule of 55 penalty free 401 K withdrawals on

Wade Pfau 09:14
No, no. There's no limit. It probably just wasn't something people are really thinking about, because this is all we're talking about in this four and a half year window between 55 and 59 I guess, if you're actively leaving employers and starting at another employer and leaving it and going to another employer, yeah, there's no limit on how many plans you could be taking distributions from. But again, in practical terms, you couldn't stay employed very long with these additional employers. So you probably don't have very large accounts or growth on those accounts, I would expect, because once you're 59 and a half, this, all this goes away, and you're allowed penalty free distributions.

Alex Murguia 09:54
And if you meant that from previous 401, K plans before 55 that wouldn't work, right? It's.

Wade Pfau 10:00
Got to be you left the employment at each each of these after 55 but in that case, yeah, you can have multiple plans that you're eligible to distribute from.

Alex Murguia 10:09
I think you would have more difficulty getting a referral from somebody to like, four or five companies. Good luck with getting a good, like, job referral.

Wade Pfau 10:23
Yeah, your resume is getting pretty busy there with this four and a half year window we're talking about

Alex Murguia 10:28
that's where, like the LinkedIn, like years, or there's these gaps, or something like, I walked the Camino in Spain for two years. All right, the uh, the fourth one does starting withdrawals at a at any particular time matter after all of your 55th year and separation of service?

Wade Pfau 10:54
Oh, and I think maybe that question is getting out like so I left company. I hadn't taken a distribution yet, and then I started at Company B. At that point, can I still take distributions from Company A? I think that's what the question is really getting at. And in that case, no, that's fine. You can returning to employment. Doesn't take away your right to take penalty for distributions from your company a plan.

Alex Murguia 11:22
I what you're saying. I was thinking if they were asking about, like, is it okay to start withdrawals in general at 55 like, you know, longevity wise, but that, I think you're right. It's more along the lines of what you were saying. Okay? And he ended it mark with, thanks for your responses and love your show. My wife and I both took the Risa and our total returns. People, good to know. Good to know. Good episode for this. Since it's a lot of, you know, withdrawals and stuff. All right, we good with that

Wade Pfau 11:52
one. Yeah, nailed it. All right.

Alex Murguia 11:55
Next question has a Roth conversion theme, and good for him. He's 35 and he's already thinking about this stuff. And this is from Kevin, Kep 190 901. Cell Block C,

Wade Pfau 12:07
yeah, I think kept one of our regular commenters on YouTube. And probably this is not the first time we've had a question. So thank you.

Alex Murguia 12:15

Thanks, Kep. Really appreciate it. All right, I'm 35 tsp will allow Roth conversions in 2026 is it smart to convert at least up to the standard deduction, or wait until December 2026 to see my rough income for the year? Or do the conversions quarterly slowly? Or rip the band aid off in January the second 2026, and deal with the tax hit. The money must come outside the TSP for conversion. Thanks, docs.

Wade Pfau 12:54
Okay, yeah. And so given they may want to do these one at a time, right? Yeah, there's a lot to unpack here, but I'm I'm assuming you're still working, like it's not a fire case where you're financially independent and retired early at 35 so if you're still working, it's the what you're really dealing with here is probably more should I make contributions to the to the tax deferred version of the plan or To the Roth version of the plan, more so than already thinking about Roth conversions. But that being said, it's always a matter of you want to pay taxes at the lowest possible rate. Can you do that now? And if so, make Roth conversions, or if you're able to take those distributions from the tax deferred account later at a lower rate, just wait until later. Now, in that regard, is it smart to convert to at least up to the standard deduction? Well, you don't. If you have no other income, like it's you always want to fill your standard deduction with something. That's part of the whole tax planning. If you don't even have enough ordinary income to fill your standard deduction. You're wasting 0% tax bracket capacity. So you always want to be able to fill your standard deduction. But I think in this question, it's safe to assume there's other ordinary income that will fill the standard deduction for you. So you don't want to do a Roth conversion to fill the standard it's you want to have your standard deduction filled somehow. If it's already filled with other income sources, you're not specifically doing a Roth conversion to fill the standard deduction. It's already been filled. And then beyond that, generally, yeah, we do look at later in the year for Roth conversions, because you really do want to get a sense of what your tax picture looks like for the year. You're not jumping on January 2 and making the Roth conversion. It's more at the end of the year. You want to look at like we have our tax map calculator at the retirement researcher Academy. You want to look at your income situation for. Of the year and see whether you have some capacity to do Roth conversions and an effective marginal tax rate that looks reasonable to you, and that's really something you can only consider at the end of the year, especially if you're going to be hitting into the preferential income stacking issue, you have to know what your qualified dividends and long term capital gains distributions for the year are going to be before you know what level of ordinary income is going to start pushing your preferential income from 0% to 15% and then that, that may be the constraint. You do enough Roth conversion to get you up to where you still have your long term gains and qualified dividends taxed at 0% and that's where you stop the $1 more they're starting to be taxed at 15% so yeah, the answer is, wait till later in the year to get a full income picture, and then consider whether you convert, convert at reasonable tax rates. That would definitely mean making sure your standard deduction is filled. But if you have other income to do that, you don't also do a Roth conversion in the amount of the standard deduction that that wouldn't automatically follow

Alex Murguia 16:13
good answer way. Thank you. Right. No good. This next question is from JJ Wardle, also Roth conversion theme, Gentlemen, thanks for this show. It's excellent. I have simple I had to throw that in their way. I had simple question for the podcast related to Roth conversions. I never really hear anyone address this question specifically. We are retired in parentheses, me, age 66 and my wife, age 63 we have not started collecting Social Security yet, but we do have pensions

and other taxable income that has us in the bottom of the 22% bracket. Even with estimated future RMDs, we will likely remain in the 22% bracket, considering that our tax bracket will likely not change once RMD start. Is it worth doing Ross conversions Now, considering there isn't a large or any tax benefit, can you maybe consider, yeah, okay, covering this on the podcast, yes, yes, and we will. I'll answer that question.

Wade Pfau 17:24
Wait, okay, yeah, well, you want to consider Roth conversions if you're going to get a tax benefit from it. So if simply you're not going to get a tax benefit from it, there's really no particular reason to do it. And indeed, so pointing out, we're pretty much in the 22% bracket today, and we think even with RMDs in the future, that may push us to realize income we don't want. Well, nonetheless, they won't be so large that they'll push us out of the 22% bracket. And to be clear, even if they did, the next bracket is 24% and that's a big bracket. I mean, a lot of capacity at 24% so even if you got pushed a little bit over the edge to 24% instead of 22% it's not that big a deal

Alex Murguia 18:08
for listening audience. What do you mean by that's a big bracket.

Wade Pfau 18:12
It's large. I mean, you can have a I don't have at the table. Oh, I do

Alex Murguia 18:17
have, well, the income, it pertains to the income spread, is what your spread of income? So the 20 you don't even know exactly, I just wanted them to think, because they may be thinking 22 to 24 is just two percentage points. What are you talking about? But it's really that you have a lot more income to play with within the 24% bracket, right?

Wade Pfau 18:34
So the in 2026 next year, the for married filing jointly, the 22% bracket is taxable income from 100 and 1000, $100,800 to 211,400 so that's not so I mean, it's more than 100,000 but the 24 bracket number, it lasts for about $200,000 from 211,400 to 403,550

Alex Murguia 18:59
and since we're on this, since I, You know, I heard you, this relates to the previous answer a little bit you had said you want to fill up your like the deductions. You want to just talk about that dynamic very briefly so they understand what you mean by that when you were referencing your deductions.

Briana Corbin 19:15
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Wade Pfau 19:39
Well, your below the line. Deduction is effectively a tax bracket too, although it's not shown on the tax tables that way, and you pay 0% it's a 0% tax bracket. So if I don't fill up my standard

deduction, I'm missing a chance to pay taxes at 0% and the whole conversation is we want we know we have. To pay taxes at some point, we look for opportunities to do it at the lowest possible rates. So if we're missing the opportunity to pay taxes at a 0% rate, it's not particularly efficient.

Alex Murguia 20:11
Yeah, you should unload as much as you can into that, into that bracket. Yeah, you always maybe have conversion opportunities. Now, if

Wade Pfau 20:20
you have other income sources that fill your below the line deduction, then where, that's kind of what the previous question. There's nothing else you can do. But if you don't have other income sources, you don't want to leave that standard deduction empty, and especially if you're 65 and older. Now with this temporary age 65 bonus deduction that we have through 2028 but yeah, the whole issue here, if you're in the 22% bracket already, it means you've already passed two of the big hurdles out there with tax nonlinearities. Well, if you had claimed Social Security, and someday you will, but you haven't yet, you're already out of the tax torpedo for Social Security, at least for the most part, unless your benefits really big, and you've also passed a preferential income stacking issue, because that happens entirely in the 12% bracket. So once you get to the 22% bracket, you're past two of the biggest hurdles. Now, the Affordable Care Act, if you're getting insurance, to the Affordable Care Act that would probably put brakes on any Roth conversions. And then beyond that, we're now through 2028 we have this age 65 plus bonus deduction for this couple. One of them is over 65 so that would be a $6,000 bonus deduction. And in the 22% bracket, you're in the phase out range for that. So right now your your effective marginal rate from that would be, I think, 24.64% so that would push you against doing a Roth conversion, because right now you're paying a higher tax rate, whereas in 2029 and later, unless they renew the extension to keep that extra deduction, you'll be back down to a pure 22% bracket. There's Irma surcharges to deal with along the path up there, with where you are in the 22% bracket, the net investment income tax kicks in at $250,000 and then well beyond that, you run into the salt phase out that we now have temporary that we talked about with Brett a few episodes back. Yeah, that doesn't begin both $500,000 so that's well beyond the 22% bracket. So yeah, all that together, if, if RMDs are not going to be pushing you into higher tax brackets, probably the balance of indications without really just sitting down and making sure to double check all the numbers. Yeah, probably there's not a particular need to do Roth conversions now at 22% to avoid future, rough future RMDs at 22%

Alex Murguia 22:56
the something I like to point out Wade, and this is from our correct marketing team. They say we don't, we don't talk about the resources that we have sometimes in a manner that that we could and as you can gather from the answers that Wade is giving a lot of the decisions to convert now versus later, has to do with bracket management and your what your ink, what your expected income is going to be this year versus maybe a future year, where it may be better to do it in the future, a conversion, as opposed to now, or vice versa. And you had mentioned that tax maps, can you discuss what we're actually, you know, just released on retirement researcher, and what you have planned for the taps tax maps? Because I fear people are listening to you, but they're also, you know, even though you're saying, if this happens and this, if that, then this, if this and that, but all those require sound calculations until you're, you're, you

know, expected tax rates for the year. And what have we created on retirement researcher to help individuals, you know, muddle through that a little bit better.

Wade Pfau 24:01
Yeah, we have the tax map calculator, and we just released a big update for it in November, including all the new provisions in the tax code, with the new deductions that phase out with income. And things got a lot more complicated. But yeah, it lets you, and that's where, at the end of the year, it's the best time to do this. It lets you input all your different income sources for the year. It lets you put in a target for the effective marginal rate you're willing to manage for ordinary income and also for preferential income. We show you both, whether it's Roth conversions or harvesting long term capital gains, it'll show you your capacity to do that still at a particular tax rate target and give you guidance about what you want to do. And so what it would show, in this case, if you're in the 22% bracket right now, you are dealing with one person, age 66 you are dealing with the phase out of $6,000 of additional below the line deduction. And, oh yeah, since it's just one, it wouldn't push you to 24.64 it pushed you to half, like 23.3 something percent as an effective marginal rate, it would be 22 times 1.06 that would be your effective marginal rate right now. That's where, if later, if that phase out ends in 2029 and later, you're back down to a 22% bracket, and then it's just really in that range, Irma, and potentially getting close to the net investment income tax kicking in. And the tax map calculator we have would show you visually all of that.

Alex Murguia 25:41
And this is available at retirement researcher.com it's a membership site where we have tons of tools and cheat sheets and things along those lines. So I encourage everyone to check it out if this is something that you've been thinking about from the standpoint of Roth conversions, but also beyond just general financial planning. It's a curated site where we have our content workshops, etc. But we also have tools that I was just thinking about it based on these questions like, well, how are they going to figure that out? And so we have plenty of tools there. Retirement researcher.com check it out. Yeah.

Wade Pfau 26:15
It's the specifically the retirement researcher Academy, yeah.

Alex Murguia 26:20
Okay. Then here we go. Let's move on to the next one. This talks about the 4% rule and qualified, non qualified accounts. But before I answer the question, just let me, for those of you listening, a qualified account is our parlance, and maybe it's too much of a jargon term, but it's, it's so ingrained in our heads that we probably say, without even thinking about qualified accounts are like tax deferred and tax free accounts, the Roth IRAs, 401, K's regular IRAs, etc. They're just called qualified accounts. Non qualified accounts are accounts that you're going to have cap gains on capital gains on accounts. Yeah, so if you're listening to like the standard Schwab account, retail account that you know, joint account that you may have with your spouse, or something like that. All right, so that being the case, I'll read the question. Research on withdrawal rates seem to favor the accounts being utilized. Seem to favor that the accounts being utilized are qualified accounts. I don't get it if I am trying to withdraw for 1k before taxes, isn't it the same whether or not I am withdrawing from a qualified or non qualified account, 401 K before taxes is the same for 1k regardless of the account type. So why the disclaimer?

Wade Pfau 27:40
40k Yeah, yeah. So it's Oh, sorry I missed

Alex Murguia 27:43
the one I would say. Who's actually putting numbers you're putting? I was thinking about 401, K's, and so he actually meant for 40,000 since I messed it up.

Wade Pfau 27:55
It's just, it's, I mean, the point is, if you're taking $40,000 out of an account. Why does it matter if it's qualified or not qualified? Is basically the question, yeah. And we might have briefly addressed this in one of our episodes with Bill bengen, but I couldn't remember for sure, and still had the question on the list. But yeah, the answer is, the vast majority of the research on sustainable spending from investments, the whole safe withdrawal rate question, the 4% rule type research ignores taxes. So it's like, you don't pay taxes. Or, more specifically, you could say, well, if it's like, if it's in a Roth, no problem. It's just you get tax redistributions. If it's in a tax deferred account, well, you pay taxes on the distribution, so your after tax spending is just the 40,000 distributed less the taxes that you paid. The problem with the taxable accounts is you have ongoing taxes on interests and dividends and any realized capital gains if they're in mutual funds and things and yeah, at a very technical sense, if you considered all those side taxes coming out of the account as part of your $40,000 distribution, that would be okay. But I don't think most people are thinking that way. The issue is, all those ongoing taxes on account cash flow distributions are lowering the growth potential of the account, so the after tax safe spending rate from a taxable brokerage account will be less than, not necessarily, less than the after tax dollars you have to spend from your tax deferred account, but, but if $40,000 is a safe withdrawal rate from a tax deferred account, and you just pay your taxes out of the 40,000 Well, you can't 40,000 is not really the safe withdrawal rate from a taxable brokerage account, because unless you're doing the all this extra work to figure out the ongoing taxation on my interest and dividends and everything has to come up. Of that 40,000 it's going to be less because of the ongoing taxes. And that's why that caveat or disclaimer is out there.

Alex Murguia 30:07
Yeah, I would also say this, and, you know, correct me if I'm wrong. And yeah, I apologize. I was looking at if he broke 40k and in my head, you know, my mind was completing it as 401, K,

Wade Pfau 30:18
you're correcting. Yeah, I was autocorrecting.

Alex Murguia 30:22
What I would say, yeah, exactly. I hallucinated. What I would say, too to that is two points. When you're doing research studies, it's damn near impossible to do it with taxes. Because of the many iterations that you would have, you wouldn't be able to really get a uniform thing across the board, because what state do you live in, even, and what are you holding, and how are this, how's this tax versus that tax? So a simplifying assumption in research, it's not that we don't think no one and no one is going to pay taxes, but it's a way to make everything, even, you know, assuming there are no taxes, and then the idea, because it will still theoretically answer the heart of the research question. And so what's left out to the individuals is just do their own mental calculation on the after tax amount, on that amount, yeah, that's why it's done. Now I say the last statement Wade, unless I'm reading this wrong, 40k before taxes is the same 40k

regardless of the account type. So why the disclaimer? I I think point blank, it's not the same because the government owns part of that 40k still in these different accounts and in different degrees. And so there is some accommodation that needs to be made.

Wade Pfau 31:42
Yeah, and so I do look at this general type of question in the retirement planning guidebook before getting into the full tax chapter itself, but just in the chapter on safe withdrawal rates, I put in some simple parameters and show like if you had a Social Security benefit, and we'll just look at if you had $2 million in an investment. Account. If and the 4% rule would work. If you had $2 million in a Roth IRA, you're still able to take out what $80,000 would be 4% of 2 million. No tax issue. If you had $2 million in a brokerage account, this is where you're having to deal with the ongoing taxes on interest and dividends. How much can you sustainably spend on an after tax basis? The after tax safe withdrawal rate I get is 3.74% and then if you had $2 million in an IRA, well now you're how much can you spend after paying taxes on those distributions too? The after tax, safe withdrawal rate I got was 3.43% so 4% with a Roth, 3.74% with a taxable brokerage and 3.43% with an IRA. In terms of after tax, sustainable spending rates, and that's with a very stylized set of assumptions to your point, all they had was a Social Security benefit and money in one kind of venture.

Alex Murguia 33:03
I imagine, where you have different allocations, then it's a different study. If you have different holdings within those allocations, it's a different study. It just, it's impossible to do a uniform study from a research standpoint.

Wade Pfau 33:16
But tax planning, well, software, financial planning, software, that's where the whole like safe withdrawal rate question in real life is kind of a side issue, because if you're running the financial plan and financial planning software, it'll be accounting for the taxes for you and looking at, can you meet the distributions and pay the taxes and not run out of money. And that's how it's going to run the calculations

Alex Murguia 33:42
Fair enough. Okay, this one's related gone

Wade Pfau 33:47
question for you, so I'll do the last question for this episode. And that my question is, what do those demographic Oh, is there a part of it missing? Say it again. I think it might have been referencing so talking about general demographic and tax trends, people are getting older. The percentage of people over 65 is increasing relative to the working age population. There's a national debt. We may have to have higher taxes in the future to cover tax bills. So my question is, what do those demographic trends and tax trends mean to equities and interest rates over the next 20 to 30 years. How should a retiree position their income and investment strategy?

Alex Murguia 34:30
This is something that came up many moons ago, too, in our in our space, it comes up when they're usually it's driven by books. There's a book written, I think Harry Dent wrote a book about the, I'm confused with, now, Ken dykewald, his age wave book. But they're, you know, Harry Dent wrote a book about the, you know, the coming doom of, you know, an aging

population. And there's been a couple of them in the last like, let's say, 15. Years. In fact, I did a quick search just how many books have there been in the last 20 or so? And there's at least 10 to 15 that I recognize the titles from. And effectively, they're sort of futurist, right, where they begin to think of scenario analysis of, oh, if this happens and this and so forth. And the bottom line that you see, is okay, doesn't take a genius to figure out that. Listen, there's a whole bunch of older people getting ready to, you know, to retire. Are retiring, as evidenced by right now that, you know, 10 to 15,000 people a day are retiring, you know, on a daily basis. And so how did the markets accommodate for that. And you know, the subsequent knock on that that happens. And what you see with these books, ultimately, is, okay, fine. They're the folks are getting older, and that's going to impact changing spending, threat trends, consumers and the like, and directionally, all of those are correct, because it's just simple math, right? But what they do get, you know, consistently wrong is the degree to which you know, the outcomes that they predict as a result manifest themselves, and they're wrong because they're aging is just a factor within what's going to happen. You still have technology. You still have just basic global politics in play. You have innovations, etc, etc. And what I would, what I've what you see is that everyone knows this information of what's going to happen, and then people adjust prices accordingly. It's not like from one day to the next, everyone realizes, oh my goodness, everyone's getting older. I got to reshape my portfolio. This is stuff that is already known. Like, you know, by by the fact that I said I did a quick search, and there were like 10 to 15 books on this in the last few years that were fairly popular. It stands to reason that this isn't coming as a surprise to anyone, and when things don't come as a surprise to anyone, it sort of gets factored in on a daily basis, similar to PES. When people say, Oh, the PES are rising, right? The PES don't go from 10 to 35 in one day, right? They march upwards. They march down or whatever. But it's sort of systematically, and people just along the way, and so that's what you end up seeing. I mean, there were, you know, out of those books, I don't want to name anyone because, you know, they're doing their best trying to give a gage, but most of them are wrong, flat out wrong in terms of the impact that that's going to have on the market, while they were right on the upcoming demographic trends. And how do I interpret that? Is just the market is a prediction. It's a sort of ongoing, sort of prediction machine with odds, and it's providing the odds on this manifesting or not. And, you know, it doesn't have to make these bold predictions about the implications, because it's, you know, these prices are adjusting along the way. And so really, I I wouldn't do anything. There is nothing to do, because I think you're gonna the timing, because then you're gonna start playing into this market timing piece of it, you know. I mean, are you put all your money in memory care facilities, you know, that kind of thing? No, I wouldn't do that, because the market already knows this. The market's already pricing this in. And so the best thing you could do, especially for the next 20 to 30 years out, is just consistently diversify your portfolio across asset classes that have, you know, expected rates of return, you know, and do that in a manner that is diversified, that gives you the best risk per unit of return for return per unit of risk that you're taking. And that's not going to be different now versus five years from now, versus 10 years from now. And it shouldn't be different from the standpoint of, hey, the 6040 portfolio, or whatever the 70, whatever the 6040 portfolio that you have now, that's going to have to be effectively, a 4060, in 10 years to accommodate for such and such. I think that's a that's a fool's errand, that's gonna that's gonna lead you astray. I think you consistently stay with what you're doing, with the assumption that I know this is happening, but so does the market, and so that's how it's priced in right now.

Wade Pfau 39:18

Okay, great, very good. And that's a wrap for this episode, but we're going to continue further Q and A working to get caught up on everything that's come in now. We're not still going to get completely caught up on this round of episodes, but we're, we're moving in that direction. So stay tuned, and we'll have more Q and A episodes on retire with style. Catch you next time. Thank you, everyone.

Briana Corbin 39:42
Wade and Alex are both principals of McLean Asset Management and retirement researcher. Both are SEC registered investment advisors located in Tysons, Virginia. The opinions expressed in this program are for general, informational and educational purposes only, and are not intended to provide specific. Advice or recommendations for any individual or on any specific securities to determine which investments may be appropriate for you consult your financial advisor. All investing comes with the risk, including Risk of Loss past performance does not guarantee future results.